No. 10293

In the United States Circuit Court of Appeals for the Ninth Circuit

R. E. LEE AND STANDARD ACCIDENT AND INSURANCE COMPANY, A CORPORATION, APPELLANTS

v.

UNITED STATES OF AMERICA, APPELLEE

ON APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE DISTRICT OF MONTANA

BRIEF FOR THE UNITED STATES

NORMAN M. LITTELL,
Assistant Attorney General.
JOHN B. TANSIL,
United States Attorney,
District of Montana.
R. LEWIS BROWN,
Assistant United States Attorney,
District of Montana.
VERNON L. WILKINSON,
S. BILLINGSLEY HILL,
Attorneys,
Department of Justice, Washington, D. C.

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OPINION BELOW

The unreported opinion of the district court appears at pages 74–76 of the record.

JURISDICTION

This is an appeal by R. E. Lee and the Standard Accident Insurance Company from a final judgment of the district court entered June 27, 1942 (R. 77–79). Notice of appeal was filed by them on September 21, 1942 (R. 79). The jurisdiction of the district court was invoked by the United States (R. 2) under section 24 of the Judicial Code, as amended, 28 U. S. C. sec. 41 (1). The jurisdiction of this Court rests on sec-

tion 128 of the Judicial Code as amended, 28 U. S. C. sec. 225 (a).

STATUTE INVOLVED

The Act of May 29, 1924, c. 210, 43 Stat. 244, so far as material, provides:

> That unallotted land on Indian reservations other than lands of the Five Civilized Tribes and the Osage Reservation subject to lease for mining purposes for a period of ten years under the proviso to section 3 of the Act of February 28, 1891 (Twenty-sixth Statutes at large, page 795), may be leased at public auction by the Secretary of the Interior, with the consent of the council speaking for such Indians, for oil and gas mining purposes for a period of not to exceed ten years, and as much longer thereafter as oil or gas shall be found in paying quantities * * *.

QUESTION PRESENTED

Whether the Secretary of the Interior has the right to insist on the drilling of the number of test wells specified in an oil and gas lease executed pursuant to the Act of May 29, 1924, c. 210, 43 Stat. 244, and, upon failure to drill the wells, to demand payment of the bond made to insure performance.

STATEMENT

On January 24, 1936, the Secretary of the Interior approved a lease made by the Superintendent of the Blackfeet Indian Tribe to R. E. Lee of certain tribal land (470 acres) near Cut Bank, Montana, for oil and gas mining purposes (R. 9–20, 60). The lease provided

that the lessee drill "at least (Four) wells on the premises within one year from date of such approval" (R. 13, 61). It further provided "that if the said lessee shall fail or refuse to drill as provided herein, or fail to obtain an extension of the time within which to drill he shall pay to the officer in charge, for the benefit of the Blackfeet Tribe of Indians, the full amount for which this lease is bonded" (R. 7, 14, 26). A bond in the amount of $6,000.00 to insure performance of the terms and conditions of the lease was executed by R. E. Lee, as principal, and the Standard Accident Insurance Company, as surety (R. 21–24, 60–61).

On December 4, 1936, the lessee applied to the Secretary of the Interior for cancellation of the lease and release from liability under the bond on the grounds that he had drilled one well which was not productive and that other developments on adjoining land were also unsuccessful which facts "point to the improbability of obtaining oil or gas by further developments or drilling" (R. 38). The lessee was notified by letter dated July 9, 1937, that he was given 30 days within which to show cause why the lease should not be cancelled and payment of the full amount of the bond demanded (R. 24–26). In answer to this notice to show cause, the lessee wrote to the Secretary of the Interior on August 12, 1937 (R. 39, 82) explaining the extent of of the drilling on the land and in the vicinity, and stating that he believed further drilling would be useless, that he understood the bond was only for the purpose of making sure that "proper drilling, casing and abandonment procedure were followed," that he believed

section 7 of the lease permitted him to surrender the lease without liability under the bond and that any other interpretation of the lease would have a "detrimental effect on the future sales of Indian lands in the Cut Bank fields" (R. 50–56).

After the matter had been "carefully considered" (R. 40) and the Indian lessors consulted (R. 40, 112), the Secretary of the Interior cancelled the lease on January 10, 1938, and held the lessee and his surety liable for the full amount of the bond (R. 21). Notice of this action by the Secretary and a demand for payment within 30 days were forwarded to the lessee and his surety on February 3, 1938 (R. 39–40). Payment not having been received, this suit was instituted in the district court on December 18, 1939, to collect the amount of the bond with interest from February 3, 1938 (R. 2–9). Judgment in favor of the United States was entered June 27, 1942 (R. 77–79). Notice of appeal from the judgment was filed by R. E. Lee and the Standard Accident Insurance Company on September 21, 1942 (R. 79).

ARGUMENT

I

By specific provisions in paragraph 4 of the lease the Secretary of the Interior reserved absolute power to insist on the drilling of at least four test wells

Since it is a matter of common knowledge that the opinions of experts differ widely as to the probability or improbability of finding oil or gas underlying a specific tract of land, it is entirely reasonable for a lessor to reserve to himself the absolute power to insist

on the only conclusive method of determining whether oil or gas underlies his property, namely, the actual drilling of several regularly spaced test wells. If he did not reserve this power as to the first lessee, then he might never have his land fully tested because each dry well would increase the risk of not finding oil or gas and would thus serve to discourage subsequent prospective lessees. Cognizant of these facts the Secretary of the Interior expressly reserved in the lease under consideration the absolute power to insist upon the drilling of a specified number of test wells or the forfeiture of the bond for nonperformance. Paragraph 4 of the lease provides (R. 13, 14):

> *The lessee agrees* to begin drilling operations on the land covered by this lease within (90) days from the date of approval hereof by the Secretary of the Interior and *to drill at least (Four) wells on the premises within one year from date of such approval:* and to drill four wells during each successive year thereafter until as many wells have been drilled as there are forty acre tracts or fractional parts thereof included in the lease; and thereafter to diligently drill such additional wells as may be necessary and proper in the judgment of the Secretary of the Interior to fully develop the land and extract the oil and gas therefrom in accordance with the most approved methods of drilling development in the field where the lands are located. It is further understood and agreed that the completion of a well is to be considered a minimum depth of one hundred (100) feet into the Madison limestone, unless production in paying quantities is found at a lesser depth. *If the*

> *lessee shall fail to drill any or all of the wells as herein provided, such failure shall be a violation of one of the material and substantial terms and conditions of this lease* and be sufficient cause for cancellation of this lease, but such cancellation shall not in any way serve to release or relieve the lessee or surety from the covenants and obligations to pay any accrued obligation: *Provided,* That the Secretary of the Interior may, in his discretion, upon application of the lessee, extend the time within which any well shall be commenced upon the payment of annual rental of one dollar per acre, for each whole year the beginning of such well is delayed. For the guidance of the Secretary of the Interior, the Blackfeet Tribal Business Council will be consulted as to its opinion in this matter. It is further understood and agreed that *if the lessee shall fail or refuse to drill as provided herein,* or fail to obtain an extension of the time within which to drill *he shall pay to the officer in charge, for the benefit of the Blackfeet Tribe of Indians, the full amount for which this lease is bonded.* * * *[1]

It is submitted that no language could more fully express an intention on the part of the Secretary of the Interior to require the wells to be drilled or the bond forfeited than that here used. The exaction of this condition was not unreasonable.[2] It must be remembered that the lessee submitted bids for the privilege of drill-

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[1] Italics supplied throughout this brief.

[2] "Although a sand may not produce in one well it may be commercially productive in an adjoining or nearby well." Bulletin No. 232, "Manual for Oil & Gas Operations", Bureau of Mines, cited in *Forbes* v. *United States*, 127 F. 2d 404, 410 (C. C. A. 9, 1942).

ing wells on the property here involved. He was seeking a privilege from the Government, the fee owner of the property in question (R. 59–60). He was not obliged to enter into any lease with the Government. Having asked for a lease, the Secretary exacted as a condition that he drill a specified number of wells in order to fully test the land included in his lease. As was said in *Fidelity & Deposit Co. of Maryland* v. *Jones,* 256 Ky. 181, 192, 75 S. W. 2d 1057, 1062 (1934), a case involving a similar oil and gas lease:

> The purpose of the lease was to drill the leased premises for oil, gas, and salt purposes, by putting down the number of wells thereon stated in the leases and within the time stated in the bonds. If it was intended by the parties that a test of the leased premises might be made by putting down wells outside thereof, the principal in the bonds and its surety should have protected themselves at the time of the execution of the bonds by a provision to that effect. They may not now rely on an implied covenant to that effect to escape their liability on the bonds. The bonds and leases evidenced the contract between the parties, and neither lessee nor its surety is entitled to declare the bonds unenforceable on the ground of the lessee's nonperformance, nor defeat a recovery thereon by alleging and proving that it can be shown by drilled wells in the vicinity of leased premises, there was at the time of either the making or breach of the bonds, neither gas, oil, nor salt in paying quantities on the leased premises.

The power of the Secretary to exact such a requirement in return for the privilege of drilling on Government-

owned property is not, and of course cannot, be questioned. Act of February 28, 1891, c. 333, 26 Stat. 794, 795, and Amendatory Act of May 29, 1924, c. 210, 43 Stat. 244; cf. *Forbes* v. *United States,* 125 F. 2d 404, 408 (C. C. A. 9, 1942).

II

The Secretary of the Interior did not bind himself in paragraphs 7 and 8 of the lease to accept less than the full test for oil or gas expressly provided by paragraph 4

The appellants contend (Br. 23, 38) that the express requirements of paragraph 4 were modified by other provisions in the lease. They contend that paragraphs 7 and 8 make it obligatory on the Secretary to accept under certain circumstances a surrender of the lease. We disagree.

A. *Paragraph 7 of the lease does not require the Secretary to accept a proffered surrender.*—Paragraph 7 of the lease provides (R. 17):

> The lessee *may, with the consent of the Secretary of the Interior,* surrender this lease in whole or in part by paying to the officer in charge all amounts then due as provided herein and the further sum of one dollar and have this lease cancelled as to the part or parts surrendered and be relieved from all further obligations or liabilities thereunder * * *.

Thus it will be seen that paragraph 7 permits a lease to be cancelled "with the consent of the Secretary of the Interior." Where consent is required the absolute power to withhold consent is implied. *State ex rel. United Rys. Co. of St. Louis* v. *Public Service Commis-*

sion of Missouri, 270 Mo. 429, 192 S. W. 958 (1917); *Rice* v. *Culver,* 172 N. Y. 60, 64 N. E. 761 (1902); *Builders Supply Co.* v. *North Augusta Elec. & Imp. Co.*, 71 S. C. 361, 51 S. E. 231 (1905).

B. *The provision of paragraph 8 incorporating general regulations does not require the Secretary to dispense with the drilling of wells provided for in paragraph 4.*—Paragraph 8 of the lease (R. 17) states that—

> This lease shall be subject to the regulations of the Secretary of the Interior now or hereafter in force relative to such leases, all of which regulations are made a part and condition of this lease.

Among the regulations then in force was Regulation 27, which provides (R. 143) that "A lease will be cancelled by the Secretary of the Interior for good cause upon application of the lessor or lessee * * *." Appellants construe this regulation as requiring the Secretary to cancel a lease where "good cause" is shown. A general regulation incorporated into the lease in this indirect fashion should not be construed as dispensing with the express requirements of paragraph 4, which, as we have seen, were incorporated for a specific purpose, namely, to insure a complete test of the property covered by the lease. Regulation 27 reserves to the Secretary the determination of what constitutes good cause. It cannot be presumed that by his own regulation the Secretary intended to transfer to the courts the exercise of his discretion in determining this question. In fact Regulation 58 discloses that the Secretary's decision "shall be conclusive." Regulations

Governing the Leasing of Tribal Lands for Mining Purposes, approved July 23, 1924; 6 Summers, Oil and Gas (1939), sec. 1013; cf. *Smith* v. *United States,* 113 F. 2d 191 (C. C. A. 10, 1940).

The appellants urge that the Secretary of the Interior was required to cancel the lease and forfeit the bond because the lessee's performance was such as would satisfy a reasonable man (Br. 36–38). It is true that the cases involving contracts in which the satisfaction of the obligor is a condition precedent to payment hold that if the obligor should reasonably have been satisfied, the condition will be deemed fulfilled. The present lease does not fall within the class of cases to which appellants refer. In addition a clear distinction is made in those cases between situations in which his *judgment* is involved and situations involving operative fitness or mechanical utility. Only in the latter situations is reasonableness made the test. One reason for this is that only the latter situations are adapted to such a test. As appellants admit (Br. 37), where judgment is involved it is too difficult to fix a standard and there is too much room for disagreement for such a test. *Bishop* v. *Bloomington Canning Co.,* 307 Ill. 179, 185, 138 N. E. 597, 599 (1923); *McCrimmon* v. *Murray,* 43 Mont. 457, 469, 117 Pac. 73, 76 (1911). As stated previously and as shown by the testimony of the lessee (R. 119), the question whether oil or gas underlies a specific tract of land is one concerning which even the opinions of experts are unreliable. Experts and reasonable men may and often do disagree as to the existence or nonexistence of oil and where they agree that it does not exist, the judgment of men considered

unreasonable often proves them wrong (cf. R. 75). Therefore, in the present case, where the question to be determined is not only one for personal judgment but one as to which such judgment may easily be wrong, appellant's own statement of the law (Br. 37) that matters involving the judgment of the promisee are excluded from the "satisfaction of a reasonable man" rule is peculiarly applicable. Moreover, even if the existence or nonexistence of oil were a matter as to which general agreement were possible, the fact that the lease involved does not make satisfaction, reasonable or otherwise, the test but specifies expressly how the property shall be tested for oil, namely, the drilling of at least four wells (R. 13), removes all doubt as to the inapplicability of the above rule. *Fidelity & Deposit Co. of Maryland* v. *Jones,* 256 Ky. 181, 192, 75 S. W. 2d 1057, 1062 (1934).

In any event the Secretary's refusal to dispense with the requirements of paragraph 4 was not arbitrary. The appellants make the mistaken assumption that the Secretary was bound to consent to the surrender unless he had facts upon which to base a refusal. The converse of that statement would be closer to the truth, namely, that he was under a duty to the Indians to refuse to accept a surrender unless he had facts before him which convinced him that it should be accepted. It was certainly not arbitrary for the Secretary to decide that the facts and opinions offered by the lessee did not overcome reasonable doubt as to the nonexistence of oil or gas (in the absence of extensive drilling).

Appellants' contrary argument (Br. 23, 38) also overlooks the fact that both the statute (R. 9) providing for the leasing of these tribal lands and paragraph

4 of the lease specifically state that the wishes of the Tribal Council of the Indians will be consulted in matters affecting the lease of their lands. The Tribal Council was consulted in this case (R. 40, 112) and it was determined that the desire of the Council that the lessee be held liable for the amount of the bond was "reasonable and should be followed" (R. 40). Therefore, even if the Secretary of the Interior had not reserved absolute power to insist on the drilling of four wells, his refusal to forfeit the bond cannot be considered arbitrary. Despite appellants' contention to the contrary (Br. 28), the desire of the Blackfeet Tribal Council that the bond be forfeited does not beg the question whether good cause was shown to the Secretary. In a matter such as this, the opinions or wishes of the Indians have a direct bearing on the question of good cause and are entitled to as much consideration as any other opinions, wishes, or facts offered to influence the decision of the Secretary. Their desires were considered "reasonable." They furnished a valid basis for the judgment of the Secretary.

It is to be noted that all the authorities cited by the appellants to support their contention that the Secretary acted arbitrarily are cases in which the court refused to override the judgment of the Secretary. The sentence succeeding the quotation used by the appellants from *Anicker* v. *Gunsburg,* 246 U. S. 110, 119 (1918) (Br. 39) reads as follows:

> But it [the statute] does give him power to consider the advantages and disadvantages of the lease presented for his action, and to grant or withhold approval as his judgment may dictate.

And on page 120 of that case the court said:

> The fact that he has given reasons in the discussion of the case, which might not in all respects meet with approval, does not deprive him of authority to exercise the discretionary power with which by statute he is invested.

The statute in the present case gives to the Secretary of the Interior the power to lease Tribal Indian lands. It leaves to his discretion every decision and every administrative detail necessary to the effective carrying out of this power. Since his decision was not arbitrary, it is not subject to review by the courts. *United States* v. *California &c. Land Co.,* 148 U. S. 31, 43 (1893); *United States* v. *Lane,* 269 Fed. 202, 204 (App. D. C. 1920); *Riverside Oil Co.* v. *Hitchcock,* 190 U. S. 316, 324–325 (1903).

III

The lessee was not excused from further performance on the theory that the subject matter of the contract had ceased to exist

The appellants contend that the lessee was excused from performance "because the presence of oil and gas was proved not to exist" (Br. 42). This contention is without merit. The subject matter of the contract is first of all the testing of the leased premises in the specific manner provided in the lease. As stated in *Fidelity & Deposit Co. of Maryland* v. *Jones,* 256 Ky. 181, 75 S. W. 1057 (1934), and in *Rice* v. *Ege,* 42 Fed. 661 (C. C. N. Y. 1890) no other test can be substituted and until it is completed the lessee is precluded from claiming that there is no oil or gas underlying the leased premises.

The caae of *Woodworth* v. *McClean,* 97 Mo. 325, 11 S. W. 43 (1889), relied on by appellants (Br. 47), is not in point. There the contract called for the sinking of a shaft upon a known vein. The depth of the shaft was by the express terms of the contract measurable along the vein and as a matter of course when the vein disappeared the contract became impossible of performance. An analogy in the present case would exist if the Madison limestone into which the lessee agreed to drill to the depth of 100 feet should disappear. Since there is no allegation to that effect there is nothing impossible nor any unforeseen difficulty in the performance of the lessee's covenants.

CONCLUSION

It is accordingly submitted that the judgment of the district court should be affirmed.

Respectfully,

NORMAN M. LITTELL,
Assistant Attorney General,

JOHN B. TANSIL,
United States Attorney.
District of Montana.

R. LEWIS BROWN,
Assistant United States Attorney,
District of Montana.

VERNON L. WILKINSON,
S. BILLINGSLEY HILL,
Attorneys,
Department of Justice, Washington, D. C.

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